RICHARD RUSSELL'S **DOW THEORY LETTERS, INC.**

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Sept. 12, DJIA 838.99; PTI 1122; A-D ratio −18.78
Sept. 19, DJIA 814.68; PTI 1107; A-D ratio −19.97

THE PICTURE: The public hates to take responsibility for its own actions. The average man can't deal with the guilt of being wrong. And this gives rise to a certain phenomenon which I will now describe.

I read dozens of advisory publications every week. Each has its strong points, each has its weak points, and each has its own individual personality. A few of these advisories specialize in **certainty**. All their pronouncements have the ring of absoluteness about them. It's as if they are speaking with the authority of the kingdom above.

But there's the fascinating part of it. There's an obvious comfort and attraction in certainty. Because the reader longs for certainty in a frightening world, he engages in a bit of self-hypnosis. "How can a man who's this SURE be wrong?" he asks himself, "How could he dare make this kind of pronouncement unless he KNOWS?" Despite years of experience in seeing god-like soothsayers make fools of themselves, despite watching numerous "lords of certainty" slide down Wall Street's shute to oblivion, I must confess that I am still fascinated when some new modern-day prophet issues his ultimate prophecy.

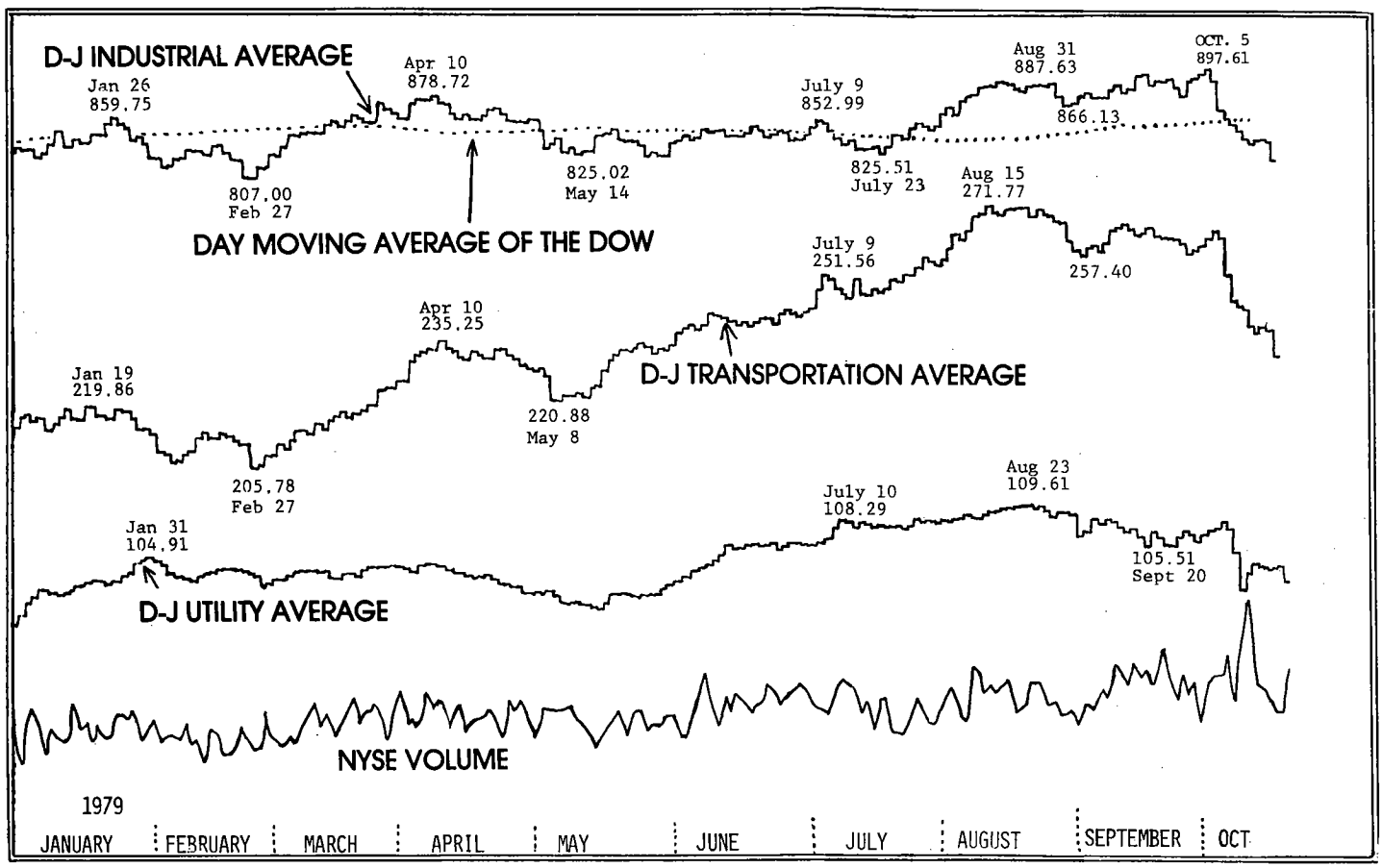
And despite the voice of experience inside me which says, "forget it, this pundit will get his Baptism of fire like all the rest," I find

FRONT PAGE COMMENT: The prime rate (the bank's lending rate to their first class customers) is now 14½%, and it may go higher. The brokerage house loan rate to margin borrowers now runs about 16½% to smaller borrowers, down to about 15¼% to larger margin users.

The compound interest tables show that at 14½% money DOUBLES in a little better than 5 years. At 16½% money DOUBLES in about 4½ years. What the compound interest tables tell me is that the squeeze is on. Consumers owe hundreds of billions. So does business. The US Government debt (forgetting the huge agencies' debt) is $815 billion. All this debt rolls over, and each issue that rolls over will have to be refinanced at the new higher rates.

What worries me is where the hell all the money is going to come from to support the debt structure at these rates! I see only one answer (assuming that this form of government is to endure), and that answer is a drastically REDUCED standard of living. There isn't enough money on the face of the earth to support today's spending and today's debts at today's levels of interest rates.

The incompetents in Washington have waited and put off, waited and put off. Finally the slumping dollar and the threats from



myself intrigued by the new champion, wondering how anyone who speaks with such conviction can possibly be wrong.

Last week I think I read about every imaginable kind of comment and prediction about the market. One adviser called this one of the great buy spots of our lifetime. Another was absolutely convinced that what we've seen on the downside so far is only the "prelude" to much lower prices. But the fact is that both men are guessing and one or both could be grossly mistaken.

The market is a story-teller, but the story unwinds gradually, and the story is often obscure. Furthermore, the story may abruptly and unexpectedly change, leaving its listeners confused or even panicked. Our job is to try to follow the story, and I know of no more difficult task. One reason why it's so difficult is that the market doesn't appreciate its audience. In fact, it will do everything it can to throw them off course.

* *

If volume of transactions alone is considered, then on the week ending October 12 the stock market suffered its worst nervous spasm in Wall Street history. When a panic occurs, the hardest thing in the world to do is put your preconceived notions, your opinions and your feelings on the sidelines and take a cold appraisal of the action. Often, the events are too emotional and too close to analyze correctly. What the days miss, the months and years may comprehend.

Let's be honest about it. Nobody alive knows the true meaning of the super-high volume crack in early October. When both Industrials and Transports violate preceding lows on very high volume, the danger bell is activated and that high volume gives the bell an authoritative ring. But the market can be deceptive, it can be very tricky, and Wall Street issues no guarantees for any signal. Yet I do know one thing–it's very comforting, and it makes sense to have "an insurance policy."

In Letter 766 (see the Addendum) I included my three progressions or "insurance levels." These were described as potential bearish signals, and subscribers were to take action if or when each successive signal was triggered. I explained that I have always considered preservation of capital as the number one duty of every investor. In this business, the ultimate sin (and the ultimate stupidity) is to lose your hard-earned, after-tax bundle.

That is the reason why I am always careful to explain what I am thinking and why. It is also the reason why I always list potential danger signals for the market, regardless of whether I am bullish or bearish.

On October 9 the D-J Industrial Average dropped below its 866.13 September low. The move was confirmed by a Transport break below its own September low of 257.40. That was danger signal number 1, and that was the point at which I advised cutting back by 1/3 to 1/2 on recent purchases.

The level of the 200-day moving average of the Dow is now 849. I stated that a decisive penetration of the 848 level would warrant unloading ½ to 2/3 of recent stock purchases. On October 12 the Dow closed at 838.99. That was 9 points below the 200-day moving average, and that is the point at which I suggested that subscribers be ½ to 2/3 out of their recent purchases.

On October 19 with the Transports slumping, the Industrial Average broke again, this time closing below the fateful 821 level. Volume expanded authoritatively on the penetration. This move triggered the final sell signal for my subscribers, and at this point I would assume that readers are on the sidelines and in protective, liquid positions.

dollar holders overseas have brought on "the big squeeze." I watched Fed Chairman Volcker on TV two weeks ago. He put on a good show. He looked tough; he talked tough. He stated repeatedly that "we're going to lick inflation."

The game is both political and economic. The current towering structure of interest rates will put tremendous pressure on the economy. The cost of running business and government and families at rates of 14% to 16% is staggering. The monetary brakes are on. And hovering over all is the shadow of the 1980 election. Will the boys in power accept a recession (possibly a very severe one) when their boss is fighting and clawing to stay in that Oval Office? The Fed has taken a strong stand. Can it back down any time soon? These are the questions the markets, and I mean the stock, the bond and the gold and commodity markets, are pondering.

I'll admit it, I've got great questions but no sure answers. Only the markets have the answers, and their answers don't look too pretty today.

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All during August and September I kept writing about that 907.74 peak on the Dow (that was the September, 1978 high). From the standpoint of Dow Theory, it particularly bothered me that the Dow failed to better that peak during its late 1979 advance. Here's why:

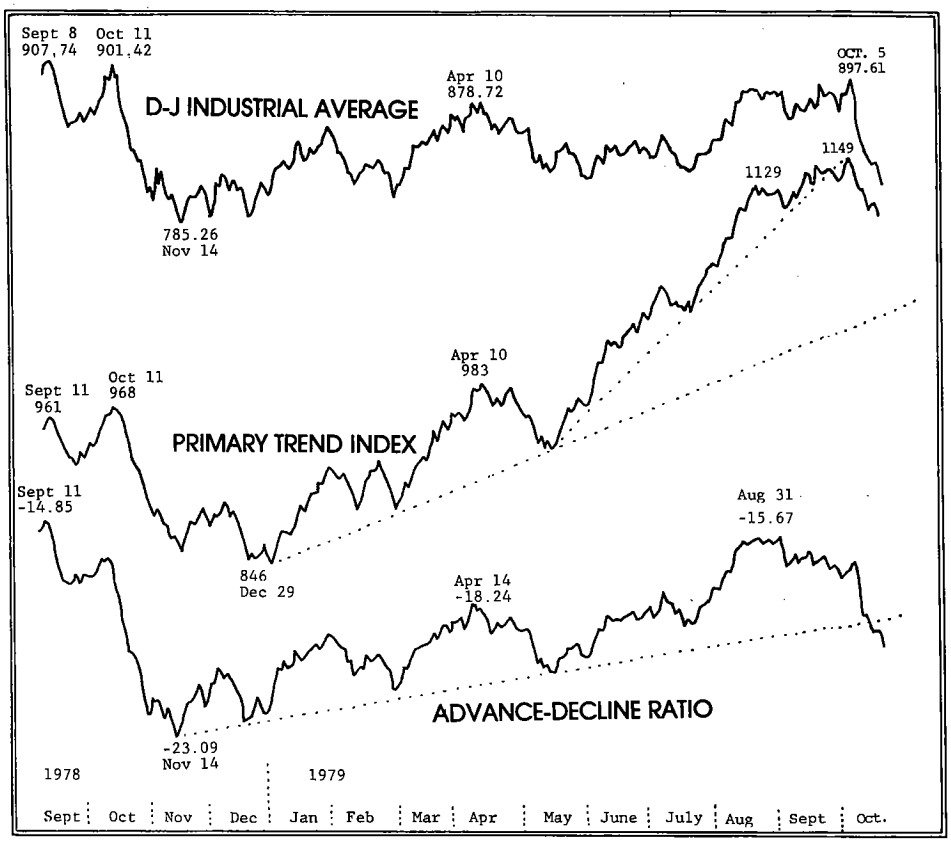
On August 15, 1979 the D-J Transportation Average (see page 1 chart) advanced to a high for the year at 271.77. This was 10 points above the 1978 Transport peak of 261.49. But in failing to confirm (i.e., failing to better 907.74), the Industrials now present us with the picture of a one-year non-confirmation in the Averages.

The refusal to better 907.74 is a problem from yet another standpoint. The Dow has failed to better its preceding year's high in every year since 1976. It now looks as if 1979 will be **another** addition to this negative series. These three failures (1977, 1978 and 1979) leave me wondering how long this can go on without precipitating a major market collapse. Or let's put it a gentler way–this latest failure by the Dow to better a previous year's high must be taken as a bearish phenomenon–and one that should not be dismissed lightly.

Readers who have been with me for a few years or more know that the market doesn't always do what I would like it to do–nor does it have to follow my script. But they also know that I attach a good deal of importance to technical "failures." The refusal of the Dow to better 907.74 was a major technical failure. Sometimes, a failure can tell us as much about the market as a success can. In this case, I take the Industrial Average's failure very seriously.

Next, let's turn from Dow Theory to a study of the Primary Trend Index (PTI) and the advance-decline ratio (see page 3 chart). The PTI is my own index. It is an amalgam of 8 critical averages and indices, and it's compiled on a daily cumulative basis. The purpose of the PTI is to gauge the weight of technical forces. If the technical forces are building up (increasing) the PTI will trend higher. If the technical forces are ebbing, the PTI will sink.

The PTI embarked on a powerful uptrend in December, 1978 (see chart). In May the uptrend accelerated, and thus we see a



steeper trendline extending through the May and July lows. The peak for the PTI was recorded on October 5 at 1149. Three days later, the steeper of the two rising trendlines was ruptured. This was the first sign of weakness in the PTI since last December.

From here on the action of the PTI should be particularly informative. If the market foundations remain weak, then the PTI should decline with the same **persistence** with which it advanced over the past year. When the worst is over, the PTI will show resistance to decline, and begin to form a base. It will be interesting to see whether, over the next month or so, the PTI can hold above its shallower trendline. In other words, I think the crucial factor is whether the PTI simply "got ahead of itself" (in which case we probably saw a technical shake-out) or whether the PTI is about to begin a persistent (bear market) voyage to lower levels.

Turning to the A-D ratio, this index measures the advancing or declining tendencies of ALL the stocks on the NYSE. In the 11 months since November, the A-D has failed to recover all the ground lost during last year's "October massacre." At its August 31 peak of minus 15.67, the A-D was one point below its peak of September 11, 1978.

The A-D decline from the August 31, 1979 peak has been in force for almost two months. The A-D has now lost about 4 points, not a severe loss so far.

In comparison, the "Massacre" of late-1978 lasted from September 11 to November 14, a period of just over two months. The A-D during that period lost 8.24 points, about twice the pointage it has lost so far in 1979.

On October 15 (see chart) the A-D broke below its 11-month rising trendline. This is not a good sign. At this juncture, the A-D and the PTI agree as to direction. But the A-D has suffered far more in extent than the PTI.

One other unhappy item took place on October 15. The negative volume index (not shown in this Letter but see Letter 766, page 4) broke to a new low under all previous lows. This constitutes another technical minus for the market. The negative volume action tells us that when volume dries up following market advances, the gains are NOT sustained. This is the reason why the A-D has been unimpressive over the past year–and it is the reason why the A-D so quickly broke its 11-month rising trend.

Conclusion: With the Dow's violation of the 821 level on October 19, subscribers received the signal to be out of all stocks and in a liquid position. There's no point in arguing with the market; it has warned us in the strongest way it can.

Question: What do you mean by a "liquid position"?

Answer: That's a good question! I'd have to say that a liquid position is Treasury bills or a cash reserve fund or any fund that is "as good as cash."

Question: When you say cash, I assume you mean dollars. Well, how good is the dollar?

Answer: Look, I pay my bills in dollars, and I can still buy three heads of lettuce here in California for a dollar. The dollar may be going down the drain, but it isn't going down tomorrow. In other words, over the short term the dollar still has purchasing power and still pays my bills–but the stock market could take a dramatic dive. Thus, liquidity as far as I'm concerned and for our purposes right now is anything in safe, short-term fixed dollars. That does not include stocks, commodities, long-term bonds, or anything else that could be up or down a good chunk by next week.

If the US Government is about to topple, if the banking system is about to go under, if this is the end of the world–well, there's nothing I can do about it. I've often said that there is a point beyond which I refuse to worry. That point is worrying about whether the dollar will exist as a currency say in November or December, 1979!

Question: Russell, on Friday, October 19 the Dow broke below 821. Would you amplify on why you think this was a bearish move.

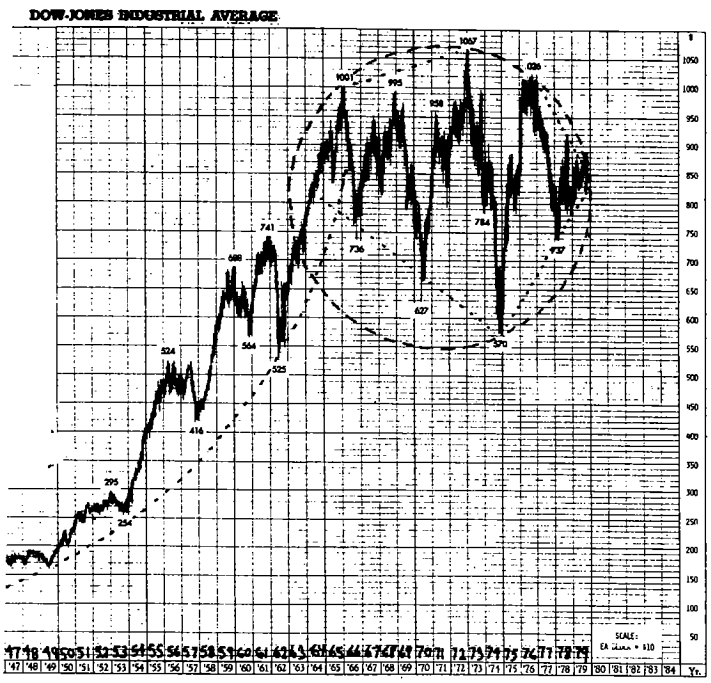
Answer: To repeat my piece about technical failures, I'll say again that what a market CAN NOT do is often very significant. Over the past 15 years the Dow has swung above and below the 821 "fulcrum level" 21 times (21 is a Fibonacci number, see Letter 764, page 2). The latest (i.e., the 21st) rally took the Dow above a well-defined triangle pattern. But instead of continuing higher, the Dow reversed and dropped back into the triangle. With the Dow now decisively below 821, my conclusion is that the latest advance above 821 has aborted. In that event, the bull forces would have failed again. Such failures are usually serious.

It is also well to remember that there is a near-record $12 billion borrowed against margin accounts on the NYSE. These margin holders are now paying 15 to 16.75% rates of interest on their accounts. If a broad slide in the market takes place, the margin holders will not only lose money via falling stock prices, they will lose money via huge margin carrying costs. Under these circumstances, a panic to sell stocks and unload margin positions could occur.

Question: Russell, in previous Letters you made much of the Dow 907.74 level and also your "great circle" concept. What do you think now?

Answer: I still consider 907.74 to be a critical point. This was the Dow high recorded in 1978. Since 1976 the Dow has never been able to better a previous year's high. Consequently, I felt that IF the Dow could better 907.74 this year that feat would be significantly bullish. The Dow hit 897.61 on October 5 (10 points under the 1978 high), then plunged. So far in 1979, we have to say that we have seen another failure.

I am reproducing my great circle chart on an up-dated basis. You can see that the Dow has pushed up to touch the upper edge of the circle but it has now fallen back. The fascinating part of this study is that by early 1980 the Dow will be out of



the circle one way or the other. What this move out of the right side of the circle portends, I do not know–yet!

Question: A lot of people are saying that the panic of the week ending October 12 (when the Dow dropped 58.62 points) followed by the slide of the week ending October 19 (when the Dow dropped another 24.20 points) have taken the market to a big over-sold low. Do you agree?

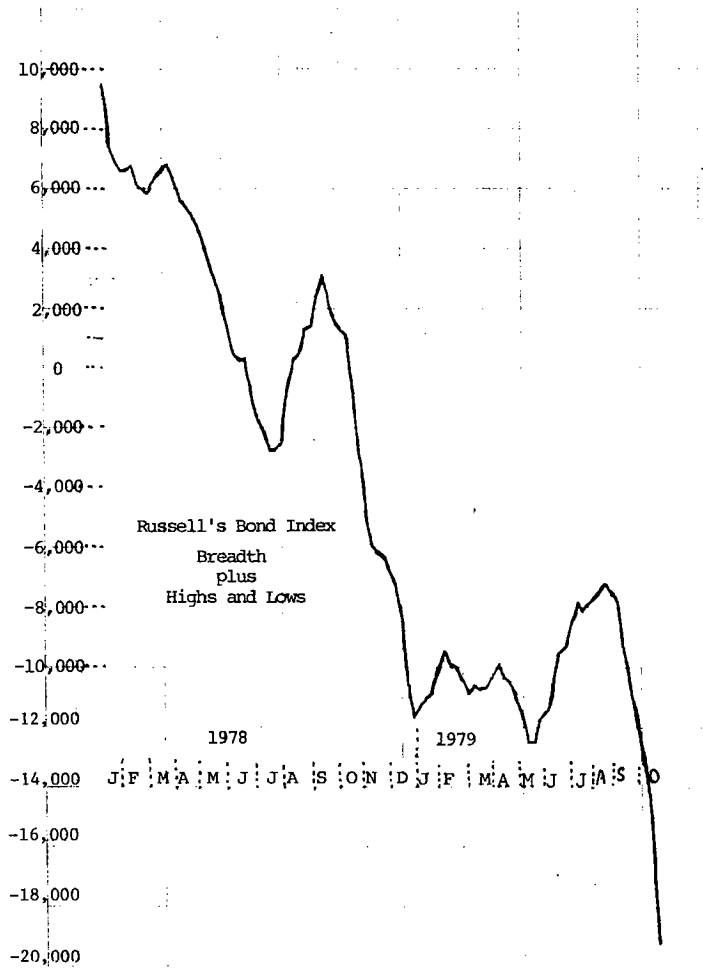
Answer: No, I don't. A few indicators sank to over-sold levels around October 12, but these were very short-term indicators. Actually, quite a bit of damage has been done to the technical structure of the market. But so far I don't detect any great feeling of urgency about selling–actually very little fear on the part of investors. This lack of fear is apparent, even though the Dow experienced its second worst week in history (in terms of points lost). The reason for the complacency, I feel, is that the bulk of the selling so far, has amounted to **profit taking.** There were many good-sized paper profits in this market, and as the market tumbled traders and investors cashed in on their profits.

Panics usually are accompanied by rising paper LOSSES. My guess is that as the 800-820 level is broken by the Dow, we will start to see paper losses build up. Under these conditions, the decline could accelerate and panic conditions could arrive (particularly if and when margins are called).

BONDS: You think you've had a hard time in the stock market, gold market, even the commodity market? Forget it, just take a look at this chart of my own bond index. This chart is a proxy for the entire NYSE bond list. It is compiled by adding daily advances and new highs (on the NYSE bonds, all of them) and subtracting daily declines and new lows. What we see here since early 1978 is one of the major bond disasters of the generation. On a shorter term basis, bonds have been in a freefall since August with no signs of a turnaround yet.

However, bonds will have their day. And when they turn, huge profits will be there for the pickings. In the meantime, the great bulk of your money (that portion which is reserved for money instruments) should be in the short term, where T-bills are paying 11.7% and some bank paper (bankers acceptances) are paying up to 14%.

Government and municipal bonds have suffered declines of absolutely shocking proportions. For instance, the bellwether Treasury 8's of 1996-2001 were over 92 only 3 months ago, in July. Last week they dropped to 82, an unbelievable loss of 11% in three months. I've been watching bonds rally and decline since



1946, but I've never seen anything like that! Long-term Governments in many cases now yield 10%. At that rate, a tax deferred pension fund can QUADRUPLE its investment in less than 15 years!

Want to know why there's pressure on the stock market? On October 18 91-day bills hit yields of over 12%. At that rate, money quadruples in a bit less than 13 years. Would you bet on the Dow going to 3440 in the year 1992? That's what it would have to do to keep up with T-bills at the current rate of interest.

But there is one consolation. In the markets, nothing (not even bonds) goes where it's going in a straight line. That means we have rallies, declines plus problems of timing. Bonds WILL rally. Inflation will ebb. Stocks will rally. The trick in today's environment is to avoid going broke between rallies!

MUSINGS: I'm 55 years of age (a Fibonacci number), and this is a strange and exotic age to be. I'll tell you why. I'm old enough to remember the "Great Depression" or at least vivid scenes from the Depression. I remember walking up Broadway in NYC (I spent my first 35 years in Gotham) and seeing "bread lines." I remember people waiting in line for bags of bread and potatoes given out by one of the political parties. I remember the shacks ("Hoovervilles") made out of tin cans, dozens of those shacks in the center of Central Park in NYC. I remember old men sleeping in caves in the Park. I remember the cold gray lines of people standing in the streets outside the employment agencies. And I remember working for the now defunct Postal Telegraph Co. for 35 cents to $1 a day. In fact, that was my first job, delivering telegrams.

My first "good" job was loading trucks for the George Button Co. in Harlem in NYC. I got $18 for a six day week, and I had to join the union to get the job. That big $18 seemed like a dream. That was the year 1940.

I remember the year 1939 when I came out to California on a Youth Hostel trip (bicycling much of the way). I saw fruit rotting on the California ground and I saw camps of hungry migrant workers. I was picked up as a vagrant (I was only 16) by the LA police, but they checked me out and I was termed OK (California didn't want out-of-state people coming in to take California jobs in those days).

I finished Horace Mann High in 1942 and enlisted in the Army. I spent three months in Infantry training and then applied for Air Force training. I ended up as a bombardier with the 12th Air Force in Italy. I saw death first hand, and I learned the meaning of stomach-freezing fear. I saw a brown-haired buddy of mine turn white-haired in one-month of combat action. I don't know why, but that sight seared itself into my brain.

I spent V-E day in Italy, and I spent my 21st birthday in North Africa. I remember thinking, "What a hell of a place for a guy to spend his 21st birthday (it was in Roberts Field in Liberia).

I got out of the Air Force in early 1945. The day after I exited I signed up for college at New York University (I had spent 1 year at Rutgers before the war). Meanwhile, I watched New York change, and I saw the streets start to fill up. By 1955 you couldn't park your car in the City, and by 1960 it was (by my reckoning) time to move.

I had grown up with Jazz and Benny Goodman at the Paramount and Billy Holiday at Kelly's Stables on 52nd Street. I went to school with Jack Kerouac and I saw the rise of the beat generation at first hand. I saw early buddies become Hollywood directors and Washington wheels and Wall Street successes and I've also seen failures and suicides and dismal tragedies. I watched Jazz turn to folk and then into rock and acid rock. I've lived life on both Coasts, although I've never really seen the center, the Mid-West. I've gone where my *instincts* have told me to go, and that's my way, and I like it and recommend it.

I could go on and on, and maybe in a future Letter I will, but what I'm leading up to is this. Today's markets are hard for a guy like me, because I remember when a buck was a buck, and the only problem was making it (not keeping it). I remember the days when $5000 a year was big money, and every young man's dream was to be a $10,000-a-year-man.

Today it s very hard for me to watch the dollar sink and gold explode and stocks fluctuate, and I realize that with a weak currency there's no anchor anymore. We buy food and clothing and pay for the movies with dollars, and yet we're sure the only safe item is gold. We see gold climb wildly in terms of dollars, and yet we know that what goes up can also come down. Thus, a man like me (who's basically NOT a gambler) has a hard time in today's markets, because the attitude one "should" really have is that of a cold, unemotional speculator.

Ideally, you and I should treat stocks and gold and dollars and copper and bank accounts and houses as just items, items that one buys and sells as the market dictates, and to hell with our emotions. Robert Rhea, the great Dow Theorist, wrote that he often felt unsure about the market, and when that feeling came over him, he would just sell out, get on the sidelines (in cash) and meditate.

It's not easy to do that today. While you're meditating the dollar could go down 4 or 5%. Or we could have a monetary crisis. What I'm trying to say is that there's no way to step aside today. There's no safe island for one's funds today. When the dollar itself is fundamentally weak, it's as if they've taken our "security blanket" away. But, I tell myself, I've lived through World War II and a hundred other disasters, and I'll live through inflation and the money-mess as well. And I will.

There's another matter that makes me wonder whether I'm still living in the past. It's this: it bothers me when my teen-age daughter leaves on the hall lights. And it bothers me when I go to the local supermarket and see them throwing out case after case of two-day old lettuce and perfectly edible beet and carrot tops. It bothers me when I see a kid buy a hamburger at McDonalds, and he unwraps about 5 separate layers of paper and cardboard, and seems to throw away more trash than the hamburger is worth.

It even irks me when I drive somewhere on a sunny California afternoon, and I see the freeways a living mass of vehicles, a never-ending roaring, raging gasoline-burning madness. "Where are they all going?" I ask myself. "How long can we keep on burning gas by the millions and millions of gallons?" And it all proves that I'm living in a different era, because who gives a damn about money or gas or paper or anything else when everything we make or possess is inflated away or taxed away? Maybe my kids have the right idea. Do what you want, work when you have to, forget about saving because you don't know what tomorrow will bring anyway.

I'll tell you a secret. I've lived the bum's life (and that's another story), and I've lived the good life. I've travelled via motorcycle and I've travelled in luxury cars. I've spent a lot of time, most of my time, pondering the markets, and I love the markets and I find them perpetually fascinating. But the ultimate quest is for your soul, not your pocketbook. Your soul is immortal, but your bank account can come and go with the price of stocks and gold and dollars.

If you can get "centered," if you can learn what's important and what is not, if you can obtain what I call "cosmic perspective" you will be way, way ahead of the game. He who lives by the sword dies by the sword. He who lives by money will die by money. Have your fun with money (as I sometimes do), but develop your perspective, your wisdom and your soul. And always speak your own truth. Maybe these thoughts will help you, I hope they do. I know one thing, they help me, and I've been a long time and a hard time coming to these conclusions.

NOTES & QUOTES: The 6th Annual New Orleans seminar (National Committee for Monetary Reform) will be held in New Orleans, Nov. 1-4. Six years ago when I spoke at the first seminar it was illegal to own gold. I remember talking to Jim Blanchard about it, and we wondered whether gold would ever be "set free." I don't know what Jim and I would have thought if we knew that 6 years later gold would jump more in 2 days than its entire "official price."

At any rate, the 6th New Orleans conference should be truly fabulous with about every speaker in the field appearing. It will be held at the Hyatt Regency, and I'll be there with Paula and little Ryan, and I'll be speaking as well. Call 504-865-9919 or 504-865-7561 for info. By the way, if you've never walked down Bourbon Street around midnight, you've got an experience coming your way!

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I don't know whether you read Playboy or not, but I read it (along with about 50 other magazines). The current issue has an excellent article entitled, "The Condominium Conspiracy" and the article is well worth pondering (the author believes the whole condominium thing is becoming a giant rip-off.) One paragraph in the article was worth repeating here. It has to do with my theory that people, at this stage, want and need inflation. Why? Because they are positioned for it.

> "To me, the risk was too great and the numbers were too high. We decided not to buy there. But in my city, the condominium craze is so bad that if you want to live in a decent area near your work, you've got to buy a condo. You either own or you get out, because all good buildings have by now been converted. That's just the way it is. So I bought a condo about a block from where we'd been renting, and I hope the market keeps going up 30 percent a year, like it has the past few years. Because with the price I had to pay for the place we bought, I need inflation to make my purchase seem sensible."

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I not only read Playboy monthly, I read the London Economist weekly. This week's issue has a great interview with Helmut Schmidt, Chancellor of West Germany. I include here a few paragraphs from the Schmidt interview:

> The world can still go to pieces economically if oil prices are managed again in the way that they have been managed by Opec countries this year; the world will not be able to digest easily another oil price explosion such as we experienced in 1979.
>
> The British are not very aware of that danger, because they have got their own oil (and if they sell some they sell it at the highest Opec prices which I don't think is prudent). But most countries, including quite a few communist countries in east Europe and, what's more important, including almost anybody in the developing world, are suffering enormous effects on their economies. Take a country like Turkey which needs about 90% of its export proceeds in order to pay for its little bit of petrol, or take a country like Brazil which nowadays needs more than one half of its export proceeds in order to pay for that little petrol. And these are just two examples—I could name a long list of countries which have been put in the greatest trouble.
>
> The repercussions of that economic trouble will also hit the British, the Germans, the French and other Europeans. The oil producers' cartel is nowadays as great a menace to the functioning of the world's economy as is the menace of governments going it the easy way by printing money and parliaments asking for more spending and less revenue. This is the way by which you are ruining empires, states, world powers.
>
> When I was a young man we had to pay 4.20DM for one American dollar. Nowadays it's 1.80DM, or something. I would like to get back into a world in which it would be two marks again and stable at that point. The world needs stability much more than anything else. But in the first instance trade unionists and entrepreneurs, and in the second instance parliaments, and in the third instance governments, all have given in to that idea of printing money.

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I'm a great admirer of Clare Boothe Luce. I would walk 10 miles to hear her speak. She gave an interview recently, and I cut this out of the interview. I thought it was interesting enough to reprint here.

> **Of President Carter—"He's a little bit of the Herbert Hoover of the Democratic Party. The problems are so infinitely complex and complicated that he certainly cannot be blamed for not being able to solve all of them, or even any of them, for that matter.**
>
> **"He inherited a horrible situation for which he wasn't entirely, or even partially responsible. But he has not been able to solve them. He has not been able to convince people that he is capable of solving them.**
>
> **"But I do not think he is as poor a leader as people think. They'll discover this if they get Mr. Kennedy."**
>
> **On Sen. Edward Kennedy—"The carry-on of the greatest American soap opera, the Kennedy family. Americans are very anxious to see all those installments about power and wealth and sex and drugs and religion, the whole 'Peyton Place' kind of story they absolutely adore. If people watch television too much they get an appetite for that kind of leader. I don't see what has qualified him (to be President). As far as I can see, his main qualification is his brothers. He has never shown leadership in any field whatsoever, except maybe welfare spending."**

GOLD: A well-known psychiatrist once defined the word "nymphomaniac" for me. "A nymphomaniac," he said, "is a woman who likes sex more than you do." Recently a gentleman asked me the meaning of the phrase, "Gold bug." I told him a gold bug is a person who has a lot of gold when you have none (and the price of gold is climbing).

The humor and irony of the situation is starting to emerge into folk lore, and I can't resist reprinting this cartoonist's version of the dollar together with a few paragraphs from a recent Art Buchwald column about a gold bug.

> "You've got to do something about Bob," she said. "He's gold crazy."
>
> "Well, if he can afford it, it's not a bad investment."
>
> "He can't afford it," she said. "He's putting everything we have into gold. He says it's the only safe thing left in the world."
>
> "Maybe he's right."
>
> "I told him I'd rather put some of it into food for myself and the children.
>
> "What did he say to that?"
>
> "He said, 'How can you think about food when South African Krugerrands are going up 5% a week?' I told him you can't eat Krugerrands, and he said, 'Maybe not today, but when gold hits $600 an ounce, we can have caviar for breakfast while everyone else will be starving to death.' "
>
> "He sounds as if he's really got the bug," I said.
>
> "Last week I told him I had to buy shoes for the children. I asked him for $50. He screamed at me, 'How can you ask for paper money when it's losing its value every day?' So I said, 'All right, give me a Mexican gold 50-peso coin instead.' He said, 'The gnomes in Geneva would really like that. They're counting on people like me getting out now, just when the market is going to soar.'
>
> "I don't know what I'm going to do. The only thing we've bought for the house in the last six months is a scale. Bob spends his evenings weighing tiny bars of gold in cellophane wrappers. When I tell him to come to bed he says, 'Not until I find out what's happened in Tokyo.' The other night I asked him, 'What has Tokyo got to do with going to bed?' and he said, 'Everything. If you watch the Japanese bankers, you'll know where the dollar is going.' "
>
> "What did you say to that?"
>
> "I said I didn't care where the dollar was going as long as I could go with it—at least to a store. He said if I just held on for six more months we could buy the store."
>
> "Where does he keep the gold?"
>
> "In the house. He took the inside out of an old television set we have in the attic. Every day he calls up from the office and asks me to go up and check to see if it's still there. He doesn't even like me to go out any more because he's afraid someone will break in while I'm gone."
>
> "Why doesn't he put it in a safe deposit box in a bank?"
>
> "Because he says the way gold is going the banks could close any day and he won't be able to get at his box."

On October 2 London gold shot up momentarily to over $440. The first fix, October 4, was $367. This was the first correction in weeks. But I might as well insert this thought. I believe gold (on this move) will record some high level, and in retrospect that will be seen as "the high." Everyone will then expect that they saw a typical bull market peak–and they will then expect a bear market to follow. I doubt that it will work that way.

I expect that following this Wave II high (and we may have seen it, I don't know), gold will fall back into a tedious trading range with Central Banks and large interests buying whenever the lower part of the trading range is approached.

Thus, the gold holder will face loss of interest while holding his gold, and this will be the penalty he will pay for holding onto his gold, rather than the penalty of a real price collapse.

Interest paid on an item is a function of risk. Since real money (gold) entails no intrinsic risk, it is a fact that gold pays no interest. The dollar, which is a managed currency, must now pay a high rate of interest. The Swiss franc, which is a well-managed currency, pays a much lower rate of interest. But it is important to understand that you generally get paid in the world of finance for the risk you take. The great bargains arrive when an item which is thought to be high risk (due to falling safety or profits) is at a fundamental turning point. Thus, for instance, important stocks in 1932 appeared to be on the verge of extinction. That proved to be one of the greatest miscalculations and therefore one of the most profitable entry points in stock market history.

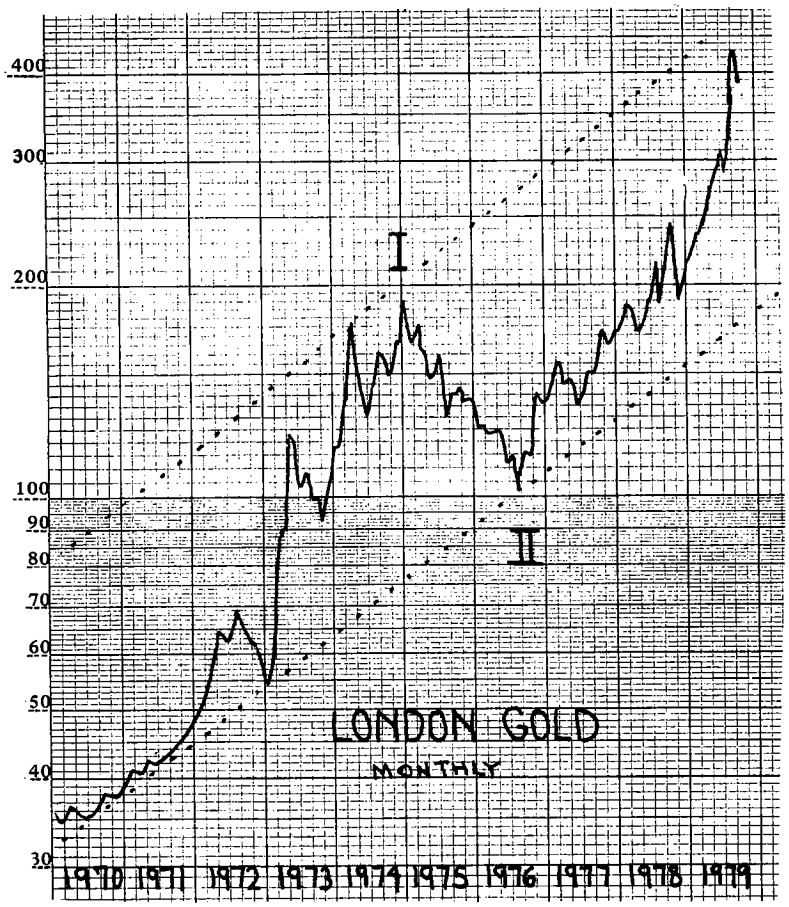
My friend Tom Holt (Holt Advisory, 277 Park Ave., NYC 10017) has a long history of liking gold and has been a strong voice in getting investors into the metal. Now he says it is time to take profits and get out. Holt feels that in view of current conditions gold is "over-valued" and probably worth around 250. Holt notes that since 1934 commodities in general have risen about 600%, gold about 1100%. He expects a lengthy correction of a year or so with gold losing maybe 150 from its current 400 level.

I believe gold is now selling with a premium built into it based on fear (based on gold's "survival value"). But I guess what bothers me about gold is the fact that it now costs so much to own it. When I say "costs," I mean gold's cost in terms of lost income via return on money instruments. With T-bills now above 12% in yield, gold would have to go to 480 in the next year to compete. I'm not saying gold can't climb to 480 in 1980, but the T-bills are a *sure thing*, and that's the problem.

I don't like guessing at markets and events so please turn to the charts on page 8. The first chart is a ratio monthly chart of gold. The first phase of the gold rise is clearly delineated. The second wave (starting from the 1976 corrective bottom at 103) may have further to go–or it could have ended at the record high fixing of 437. We just can't know at this time.

The point & figure chart tells us a bit more. Each box on this chart equals 4 points and only rallies and declines of 12 points or more are shown. The peak of the rise was recorded at the 436 box. The price then broke to the 372 box. Twice the 372 box held. Then a rally took gold to the 408 box. Since then each rally in gold has been less impressive.

It would require a move to 412 on the upside to put gold in a position to mount another attack on the 437 high. On the other hand, a drop to 368 would clearly complete this toppy looking structure. If that happened, I would say that Tom Holt would be well on his way to being right. For if gold breaks below 368, there is little support under it (see chart) until the 300 area.



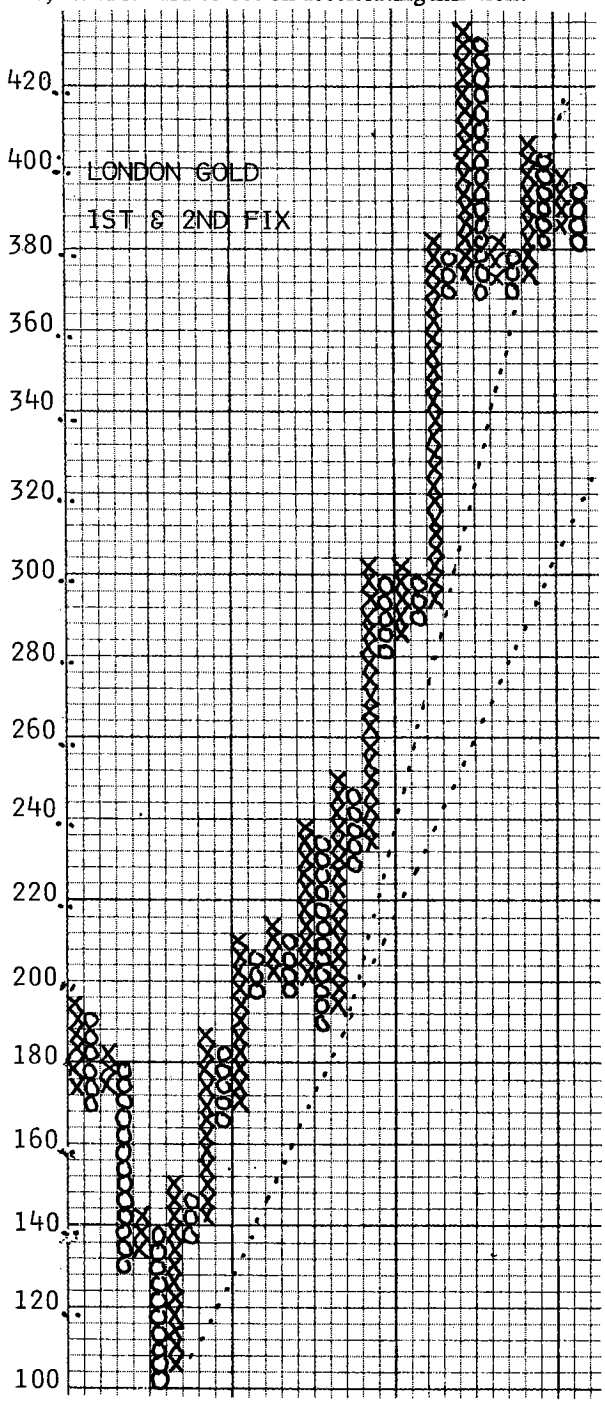
At this point each subscriber must make a personal decision regarding gold. Those who hold gold as a survival vehicle and are willing to hang onto it no matter what, those people should ignore all price movements. Because whether gold rises to 800 or drops to 200 is not their concern. Their concern is to hold a portion of their assets in real money, money that is not "managed" by politicians.

Those who like to trade gold will have to watch the 380 and 368 levels. If gold declines to 380 (spot), it will be in line to test 368. If 368 is hit, the chart will imply that a major top has been completed. Note that the steeper of the two rising trendlines has now been broken, and all gold's action is now taking place on the underside of the steeper trendline.

My weighted (exponential) 5-week average for gold is now 386 while the 13-week average is 353. The differential between the 5 and 13-week moving averages for gold hit a high at 36.65 points the week of September 28. It has now dropped for 3 successive weeks. This is a very sensitive sign of weakness in the gold price–actually it represents a drop-off in the upward rate of momentum.

The trend of gold in the period ahead will depend very much on whether inflation accelerates or simmers down. I've heard excellent arguments on both sides. The latest Value Line (they're long-term bullish) made me blink and take notice. Here's what they say: ". . *the draining of bank reserves from the monetary system, which is now underway, can be expected to brake an already slowing economy; it will retard business activity, endanger marginal corporations, result in additional consumer bankruptcies and leave the residential building market in disarray. Short-term interest rates may well rise to the 14% to 17% range but are expected to crest by the end of the year, or early in 1980, when nationwide inventory liquidation and plant closings, following on the heels of furthering slackening consumer demand during the Holiday selling season, result in a slough off in credit demands. . . The unemployment rate is likely to rise. . . perhaps pushing well above 8% to 9% by Spring.*" Value Line looks for a 20% to 25% drop in corporate profits from top to bottom.

As I say, Value Line likes to be bullish. If their predictions are true, I find it hard to bet on accelerating inflation!



I'll be in New Orleans for 4 days, and this necessitates my writing and sending the next letter two days later than usual. It will be mailed on November 9th.